



## 306 – PERFORMANCE BOND

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Staff responsible for policy: DHCM Finance

### I. Purpose

This policy applies to all Health Plans and Program Contractors that require a Performance Bond.

The AHCCCS Request for Proposal (RFP) requires the posting of a Performance Bond (PB), Section D, as long as the Contractor has AHCCCS-related liabilities of \$50,000 or more outstanding, or 15 months following the effective date of their contract, whichever is later, to guarantee (1) payment of the Contractor's obligations to providers and non-contracting providers and (2) performance by the Contractor of its obligations under this Contract.

### II. Definitions

1. United States Treasury Notes & Bonds  
This type of security is backed by the full faith and credit of the United States Government. These are notes with maturities ranging from two to thirty years. Interest is paid semiannually on the anniversary of the issue date and six months later. They are considered coupon securities even though they are now mostly issued in book entry form. Ownership is simply entered in the computers of the Federal Reserve. Interest is paid by the Federal Reserve issuing credits to the member banks that the notes are recorded through, and the banks credit the customer's account.
2. United States Treasury Bill (T-Bills)  
This type of security is backed by the full faith and credit of the United States Government, just like the Notes and Bonds. The only differences are that T-Bills are much shorter in term, three and six months, and they are sold at a discount. This means that less than the face amount is paid at original purchase and the face amount is recovered at maturity. The interest earned is part of the face amount and is earned on the amount paid for the T-Bill.
3. Federal Farm Credit Banks Funding Corporation (FFCB)  
The FFCB is 37 banks that issue two types of securities that can be substituted for the PB, Consolidated Systemwide Bonds and Consolidated Systemwide Notes. The securities are the joint and several obligations of all 37 member banks of the FFCB. It is felt that Congress will not allow this alliance to fail because of the farming community's dependence for funds.
4. Federal Home Loan Banks (FHLB)  
The FHLB serves the same function for the Savings and Loan industry as the Federal Reserve for the banking industry. It is owned by the member Savings and Loan and issues coupon bonds much like the Federal Reserve.



5. **Federal National Mortgage Association (FNMA)**  
The securities issued by FNMA are often called “Fannie Mae’s”. FNMA issues two types of securities, bonds and mortgage bonds. The coupon interest bonds are the securities acceptable for the PB. The mortgage bonds are not acceptable because of the repayment of the principal over the life of the bonds.
6. **Federal Home Loan Mortgage Corporation (FHLMC)**  
The securities issued by FHLMC are often called “Freddie Mac’s”. Bonds issued by FHLMC are mortgage type bonds that are repaid to principal and interest over the life of the bond, and the mortgages that secure the bond. This causes the principal to draw down over the life of the bond, and the life of the PB.
7. **Government National Mortgage Association (GNMA)**  
The securities issued by GNMA are often called “Ginnie Mae’s”. Bonds issued by GNMA are mortgage type bonds that are repaid to principal and interest over the life of the bond, and the mortgages that secure the bond. This causes the principal to draw down over the life of the bond, and the life of the PB.
8. **Municipal Bonds**  
Bonds issued by a municipality. The two types are General Obligation Bonds, backed by the full faith and credit of the issuer, and Revenue Bonds, repaid by the revenue generated by the project the bonds fund. Recent bankruptcies of some cities and the fact that most of these bonds are not insured makes repayment of principal somewhat endangered.
9. **Corporate Bonds**  
The most common form of bonds this category represents is debentures. Debentures are bonds drawn on the general credit and good name, of the issuing company. Rating services, Moody and S&P, and reporting companies, Dun and Bradstreet, try to continually assess the bonds value, and their issuing companies, but are limited to historic data. In the case of D&B the rating of America West Airlines was rated as good up to two months before the company filed for bankruptcy protection. This causes most users of the services to become aware of critical situations only after it is too late to do anything. This is another category of securities that is considered a good investment but does not meet the much higher standards that need to be applied in meeting the PB.
10. **Commercial Paper**  
Short-term notes issued by corporations that are much like corporate bonds. The major difference is that commercial paper must be issued for less than 270 days; this allows the corporation to avoid registration of the security. Being like corporate bonds, commercial paper holds the same drawbacks but with no advantages as a PB for AHCCCS. Also, because these notes are short-term they do not lend themselves to the 15 month time frame required by the PB.
11. **Stocks (Equity Investments)**  
Stocks, even in the most stable credit worthy companies, vary in value every day. This would require a considerable cushion above the required PB amount to compensate for market fluctuations. Also it would require AHCCCS to monitor the value of each stock posted as a PB.



This would require the resources normally found only with large investors or brokers. This monitoring is well beyond the intent of the PB.

12. Banker's Acceptance (BA)  
Bankers' Acceptance are notes from other than a bank that are guaranteed by the issuing bank. They are short-term in nature, less than 270 days to elude regulation.
13. Mutual Funds  
Mutual Funds are an equity ownership in the fund rather than ownership in any of the securities held by the fund. The principal may be in jeopardy of loss through the mutual fund's investment losses or administration expenses. Even when the fund is dominated by or wholly made up of treasury securities the fund's owner does not own the securities.

### III. Policy

Per Contract with AHCCCS, Section D, the initial amount of the Performance Bond to be equal to 80% of the total capitation payment expected to be paid in the first month of the new contract, or as determined by AHCCCS. Thereafter, AHCCCS shall evaluate the enrollment statistics of the contractor on a monthly basis and determine if adjustments are necessary in accordance with the *Performance Bond and Equity Per Member Policy*.

The following are general requirements for all PB's:

1. The amount, duration or scope of the PB may not be changed or discontinued without prior approval of AHCCCS Division of Health Care Management (DHCM).
2. A contact person must be listed and their phone number.
3. Any security agreement must be disclosed.
4. AHCCCS will confirm the PB with the appropriate institution at least annually.

Listed are several specific ways to satisfy the PB:

1. Cash Deposits, or
2. An Irrevocable Letter of Credit issued by:
  - A. A bank insured by the Federal Deposit Insurance Corporation, or
  - B. A savings and loan association insured by the Federal Savings and Loan Insurance Corporation, or
  - C. A credit union insured by the National Credit Union Administration, or
3. Surety Bond of standard commercial scope issued by a surety or insurance company doing business in Arizona, or
4. Certificate of Deposit, or
5. County resolution, or
6. An acceptable substitute in lieu of one of the above agreed to by AHCCCS.

### Cash Deposit

#### I. Deposit of Funds



- A. Any funds to be deposited with the State Treasurer shall be sent to the AHCCCS Division of Health Care Management (DHCM) in the form of a check. Along with the check should be a letter describing:
  - 1. The application of funds (Acute, ALTCS or any combination of both),
  - 2. A primary contact and phone number, for any issues concerning the deposit, and
  - 3. Instructions for the interest from the deposit: interest to be disbursed must also include directions of where the interest is to be sent.
- B. After the funds have been deposited, AHCCCS DHCM will send a copy of the State Treasurer's "Securities Safekeeping" form that records the deposit.
- C. Based on instructions with the deposit, a warrant will be issued each month for the interest on the account.
- D. The State Treasurer will furnish statements of the account only upon written request. This request may be made at any time.

## II. Withdrawal of Funds

- A. To withdraw principal funds, send a letter to AHCCCS DHCM requesting the withdrawal. The letter must include:
  - 1. The amount of the withdrawal
  - 2. The program that the funds are being withdrawn from (Acute or ALTCS)
  - 3. The date that the funds should be withdrawn, (allow a minimum of ten working days)
  - 4. The manner the warrant from the State Treasurer's office is to be handled:
    - a. Mailed by the US Postal Service, or
    - b. Courier pick-up (please include a phone number of the primary contact so prompt notice can be given), or
    - c. Wiring instructions.
- B. AHCCCS DHCM will forward the warrant in the manner requested in the withdrawal letter.



## **Letter of Credit**

### **I. Establishment of Letter of Credit**

- A. Before a Letter of Credit can be accepted as a PB it must be approved by AHCCCS for form and amount. Requirements include:
  - 1. Be of standard commercial scope and issued by a bank, credit union or savings and loans doing business in the State of Arizona and insured by the appropriate Federal Institution;
  - 2. For an amount that meets or exceeds the PB dollar requirement;
  - 3. For a time period that meets or exceeds the AHCCCS contract term plus three months;
  - 4. AHCCCS DHCM must receive a signed extension 30 days prior to the expiration date;
  - 5. A statement that the PB cannot be changed in the amount, duration or scope, or discontinued without the authorization of AHCCCS DHCM.
- B. Send a copy of the agreement to be executed to AHCCCS DHCM thirty working days prior to the execution date. AHCCCS will review the agreement and advise of acceptance or that changes are necessary. The AHCCCS review will only be for issues that are necessary for the AHCCCS PB; it will not include review for any other matters.
- C. AHCCCS DHCM will forward the letter of credit to our outside counsel for review.
- D. AHCCCS DHCM will respond in writing that the PB is acceptable or changes need to be made for acceptance.
- E. After the agreement is executed, send a statutory notice of deposit form and the original to AHCCCS DHCM. The original will be held in safe keeping until the agreement ends or is terminated by the parties. Make copies for your file prior to sending the original to AHCCCS DHCM.

### **II. Return of Letter of Credit original**

The original Letter of Credit will be returned to the makers upon:

- 1. Termination of the Letter of Credit, or
- 2. Termination of the AHCCCS contract, or
- 3. Satisfying the PB requirement with another acceptable form as outlined by AHCCCS,
- 4. Statutory Notice of Release form



## **Surety Bond**

### **I. Establishment of Bond**

A. Before a Surety Bond can be accepted as a PB it must be approved by AHCCCS for form and amount. Requirements include:

1. Be of standard commercial scope and issued by a bank, credit union, savings and loans, or insurance company authorized to do business in the State of Arizona and insured by the appropriate Federal Institution;
2. For an amount that meets or exceeds the PB dollar requirement;
3. For a time period that meets or exceeds the AHCCCS contract term plus three months;
4. AHCCCS Division of Health Care Management (DHCM) must receive a signed extension 30 days prior to the expiration date;
5. A statement that the PB cannot be changed in the amount, duration or scope or discontinued without the authorization of AHCCCS DHCM.

B. Send a copy of the agreement to be executed to AHCCCS DHCM thirty working days prior to the execution date. AHCCCS will review the agreement and advise of acceptance or that changes are necessary. The AHCCCS review will only be for issues necessary for the AHCCCS PB; it will not include review for any other matters.

C. AHCCCS DHCM will forward the surety bond to our outside counsel for review.

D. AHCCCS DHCM will respond in writing whether the PB is acceptable or changes need to be made for acceptance.

E. After the agreement is executed, send a Statutory Notice of Deposit form and the original to AHCCCS DHCM. The original will be held in safe keeping until the agreement ends or is terminated by the parties. Make copies for your file prior to sending the original to AHCCCS DHCM.

### **II. Return of Surety Bond original**

The original Surety Bond will be returned to the makers upon:

1. Termination of the Surety bond, or
2. Termination of the AHCCCS contract, or
3. Satisfying the PB requirement with another acceptable form as outlined by AHCCCS, or
4. Statutory Notice of Release



## **Certificate of Deposits**

### **I. Types of Certificate of Deposits**

Only Certificates of Deposit from banks, savings and loans, or credit unions and insured by the appropriate Federal institution, are applicable for the PB.

### **II. Assignment to Arizona State Treasurer**

All Certificate of Deposit must be assigned to the Arizona State Treasurer in compliance with Arizona Revised Statute Section 35-155. This can be accomplished with the “Assignment to Arizona State Treasurer” form.

### **III. Deposit of the Certificate of Deposit**

- A. Send or deliver the original Certificate of Deposit (or receipt for the Certificate of Deposit if a certificate is not issued) and the Assignment form to AHCCCS DHCM. A letter should accompany the Certificate of Deposit describing the form of PB the Certificate of Deposit is satisfying (Acute or ALTCS) and a contact person. Also, a Statutory Notice of Deposit form should accompany the Certificate of Deposit.
- B. After the Certificate of Deposit has been sent to the State Treasurer, AHCCCS DHCM will send copy of the State Treasurer’s “Securities Safekeeping” form to record the deposit of the Certificate of Deposit.
- C. After the Certificate of Deposit has been deposited with the State Treasurer it is the Health Plan’s responsibility to monitor the maturity date. No notification should be expected from the State Treasurer’s office or AHCCCS DHCM. Evidence of the renewal of each CD must be sent to AHCCCS DHCM within 5 days of the renewal date.

### **IV. Withdrawal of a Certificate**

Send a letter to AHCCCS DHCM requesting the release of a specific Certificate of Deposit giving:

- 1. The institution of the Certificate of Deposit,
- 2. The certificate number,
- 3. The amount of the Certificate of Deposit,
- 4. The program the Certificate of Deposit is being withdrawn from,
- 5. The manner the Certificate of Deposit is to be returned to the Plan,
- 6. A contact person, and
- 7. Statutory Notice of Release form.



## **Securities**

### **I. Acceptable Securities**

The following list is an outline of the acceptable and unacceptable securities that may be posted as a PB. The listing is not comprehensive but it includes the most common securities.

#### **Acceptable:**

- A. United States Treasury Bills
- B. United States Treasury Notes
- C. United States Treasury Bonds
- D. Federal Farm Credit Banks Funding Corporation Bonds
- E. Federal Home Loan Bank Bonds
- F. Federal National Mortgage Association (Fannie Mae) Coupon Interest Bonds

#### **Unacceptable:**

- A. Federal Home Loan Mortgage Corporation
- B. Government National Mortgage Association
- C. Municipal Bonds
- D. Corporate Bonds
- E. Commercial Paper
- F. Stocks
- G. Letter of Credit from other than a bank, savings and loan or credit union
- H. Bankers Acceptance
- I. Mutual Funds

### **II. Deposit of Security as Performance Bond**

- A. Execute a “Statutory Deposit Custody Agreement” with the State Treasurer’s appointed custodian.
- B. The face amount of the security or principal amount of the purchase price, whichever is lower, must be equal to or greater than the PB requirement. On an ongoing basis, the lower of cost or market must be equal to or greater than the PB requirement.
- C. After deciding on one of the securities to be used as a PB, fill out a “Notice of Statutory Deposit Delivery” form and submit the form and security if not in Book Entry form, to AHCCCS DHCM. Include a letter that details the reason for the deposit of the security and a contact person.
- D. AHCCCS DHCM will forward the Notice of Statutory Deposit Delivery form (and security if applicable) to the State Treasurer’s appointed custodian who will then,
  - 1. Effect the transfer from the purchasing agent, or
  - 2. Make the purchase as directed





- E. The security will remain in the safekeeping of the State Treasurer's appointed custodian. Any interest distributions will be accomplished through instructions to the appointed custodian and require no intervention by AHCCCS DHCM. (Only interest on Coupon Interest Bonds is available for distribution, interest on Discount Interest Bonds must remain in the account to satisfy the maturity amount).
- F. Confirmation statement to be received by DHCM from State Treasurer's appointed custodian acknowledging transaction completed.

**III. Release of Security as a Performance Bond**

- A. Fill out a "Notice of Statutory Deposit Release" form and send it along with a letter of explanation to AHCCCS DHCM.
- B. AHCCCS DHCM will forward the Notice of Statutory Deposit Release form to the State Treasurer's appointed custodian. The custodian will then release the security in the manner instructed in the Notice of Statutory Deposit Release form.

**IV. References**

Acute Care Contract, Section D